



MEMORANDUM

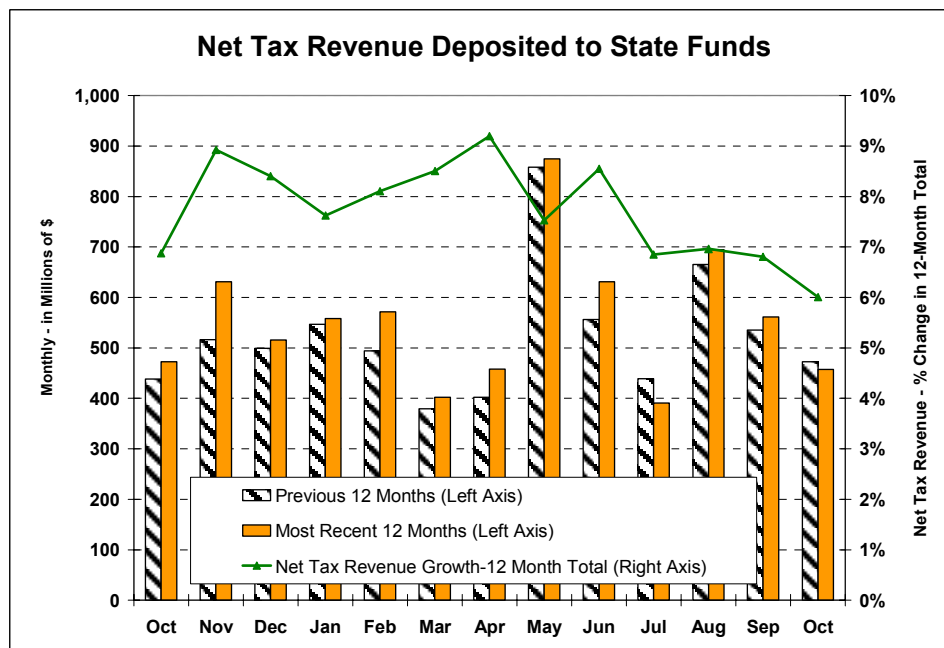
TO: Members of the Iowa Senate and
Members of the Iowa House of Representatives

FROM: Jeff Robinson
Shawn Snyder

DATE: November 24, 2008

Twelve-month Total Net Tax Receipts Through October 31, 2008

The attached spreadsheet presents net State tax receipts for the 12-month period ending October 2008 with comparisons to the previous 12 months. October 2008 to October 2007 one-month comparisons are also presented. The source of the information is the State accounting system, including non-General Fund accounts. All accounting transactions related to taxes remitted to the State were collected, along with the refunds issued against those taxes.



Month of October Comparison

October net tax receipts totaled \$457.3 million, a decrease of \$15.0 million (- 3.2%) compared to October 2007. Major taxes contributing to the month's change include:

- Individual Income Tax (negative \$9.6 million, - 4.6%) – October 2008 marks the first drop in net Individual Income Tax receipts since April 2007. Gross receipts were down \$2.1 million while Income Tax refunds were \$7.5 million higher for the month.
- Corporate Income Tax (negative \$22.6 million, - 85.6%) – Gross receipts decreased \$13.1 million and refunds increased \$9.5 million.
- Sales/Use Tax (positive \$9.2 million, 6.8%)
 - Road Use Tax Fund Use Tax deposits increased \$4.5 million.
 - Department of Inspections and Appeals Use Tax deposits decreased \$1.6 million.
 - General Fund Sales/Use Tax receipts increased \$34.1 million and refunds issued for the month increased \$27.8 million (net increase of \$6.3 million). The large increases in gross receipts and in refunds are related to the recently-enacted Statewide Sales/Use Tax increase for school infrastructure coupled with the elimination of the local Option Sales Tax for school infrastructure. This change boosts State Sales/Use Tax receipts while increasing tax refunds by a similar amount, as the school infrastructure revenue is being removed from the State General Fund through a refund appropriation.
- Fuel Tax (negative \$2.0 million, - 4.7%) – Gross Fuel Tax revenue decreased \$2.8 million while refunds processed in the month decreased \$0.8 million.
- Cigarette & Tobacco Taxes (positive \$0.8 million, 3.5%) – The Cigarette Tax was increased from \$0.36 per pack to \$1.36 per pack on March 16, 2007. The rate for other tobacco products also increased. Since reaching the one-year anniversary of increased revenue from the rate increases, Cigarette and Tobacco Tax revenue has shown positive growth for four of six months.
- Gambling Taxes (positive \$5.7 million, 24.4%) – Gambling tax revenue is deposited once per week. October 2008 had five deposit days while October 2007 had only four. This calendar issue accounts for the large monthly increase and it should reverse in November.

Year-over-Year Comparison – Net Tax Revenue

During the 12-month period ending October 2008, net revenue from all taxes deposited to State funds totaled \$6.746 billion, an increase of \$381.9 million (6.0%) compared to the prior 12 months. Major contributors to the year-over-year dollar and percentage changes include:

- Individual Income Tax (positive \$153.0 million, 5.6%) – The rate of Individual Income Tax receipt growth has decreased significantly since peaking in April 2008 at 11.8% year-over-year.
- Corporate Tax (positive \$10.5 million, 3.2%) – Corporate Tax has shown strong growth since 2003. Due to increased Corporate Tax refunds and slowing deposits, the rate of growth has tapered off over the year but still remains positive.
- Sales/Use Tax (positive \$127.8 million, 6.0%) – Despite gas prices that averaged almost \$0.90 per gallon higher year-over-year, slowing employment growth, declining home equity withdrawals, and reduced home construction, General Fund Sales/Use Tax receipts continue to show strength.
- Motor Fuel Tax (negative \$13.7 million, - 3.0%) – Net Motor Fuel Tax revenue has been weak the past nine months, likely the result of higher fuel prices reducing the growth in fuel demand. According to Department of Revenue taxable gallons sales reports, over the most recent 12-month period Iowa gasoline/ethanol gallons sold decreased 3.1% while diesel sales were 0.4% higher.

- Gambling Tax (positive \$13.3 million, 4.6%) – The new Waterloo casino and changes to the Clinton casino are boosting year-over-year statewide Gambling Tax growth. According to Racing and Gaming Commission statistics, eight of Iowa's seventeen casino/track locations reported negative adjusted gross revenue growth over the most recent 12-month period compared to the previous period.
- Cigarette and Tobacco Tax (positive \$67.1 million, 35.9%) – Over the next six months, the year-over-year rate of revenue increase will continue to decline as the second anniversary of the tax increase approaches.
- Insurance Premium Tax (positive \$9.7 million, 9.9%) – The Insurance Premium Tax rate was reduced over multiple years and is now fully implemented.

Tax Spotlight – Individual Income Tax

Iowa individual income is taxed under the authority of Chapter 422, Division II, Code of Iowa. The Iowa Individual Income Tax is imposed on Iowa taxable income of individuals, estates and trusts. Individuals who have a combined net income of less than \$13,500 (\$9,000 for single taxpayers) are not generally required to pay Iowa income tax or submit an Iowa income tax return. This "filing threshold" does not apply to taxpayers claimed as dependants on another tax return. Iowa uses federal adjusted gross income as the initial point for tax calculation.

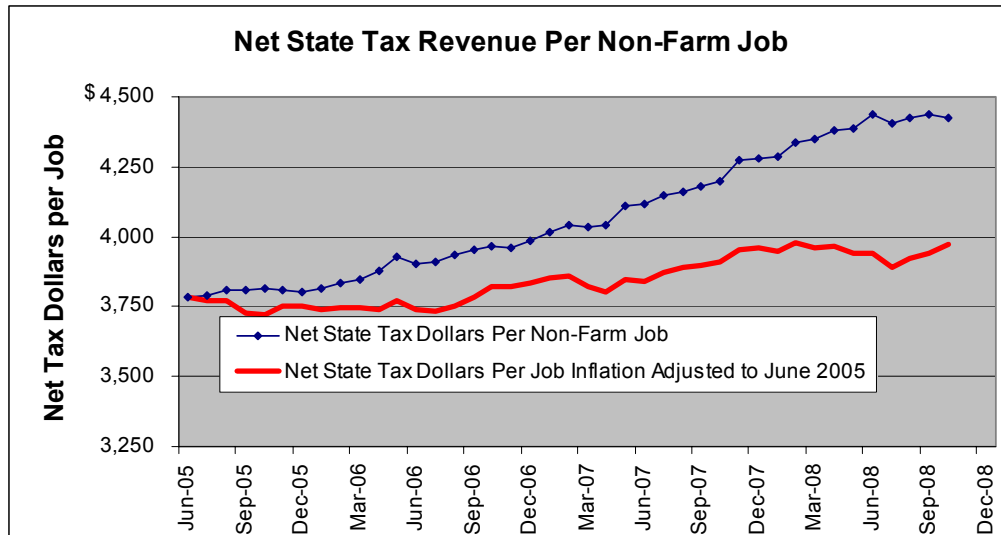
The Iowa Individual Income Tax was first imposed in 1934 with a minimum marginal rate of 1.0% and a maximum marginal rate of 5.0% (HF 1 - Income, Corporation, and Sales Tax Act). The current tax rates were established in 1998 (HF 388 – Individual Income Tax Rates Act) and are applied to nine taxable income brackets ranging from a minimum marginal tax rate of 0.36% and a maximum marginal tax rate of 8.98%. The taxable income brackets are adjusted each year by the Department of Revenue based on an inflation factor. For the 2008 tax year, the maximum marginal tax rate applies to taxable income above \$62,055. Taxpayers deduct 100.0% of federal Income Tax paid when calculating taxable income. An alternative minimum tax may be imposed at an effective rate of 6.7% if it exceeds the individual, estate, or trust's regular tax liability.

There are a large number of tax credits that may provide a reduction in Individual Income Tax. A complete list is located at <http://www.state.ia.us/tax/taxlaw/Taxcredits07.pdf>. Enactment of SF 590 (Iowa Earned Income Tax Credit Act of 2007), increased the Iowa Earned Income Tax Credit from 6.5% to 7.0% of the federal credit and made the credit refundable beginning in tax year 2007.

Individual income tax returns are filed by the last day of the fourth month following the end of the tax year (April 30). In some cases, individuals may be required to remit quarterly estimated tax payments. Withholding tax is due monthly, semimonthly, or quarterly, depending on the total amount of income tax withheld. In general, Individual Income Tax revenues are deposited in the State General Fund. Pursuant to Section 422.16A, Code of Iowa, up to \$4.0 million from withholding tax is deposited in the Workforce Development Fund each year. Section 422.100, Code of Iowa, requires that withholding tax receipts of \$650,000 each quarter (\$2.6 million annually) are credited to the Child Care Credit Fund.

Tax Revenue and Employment

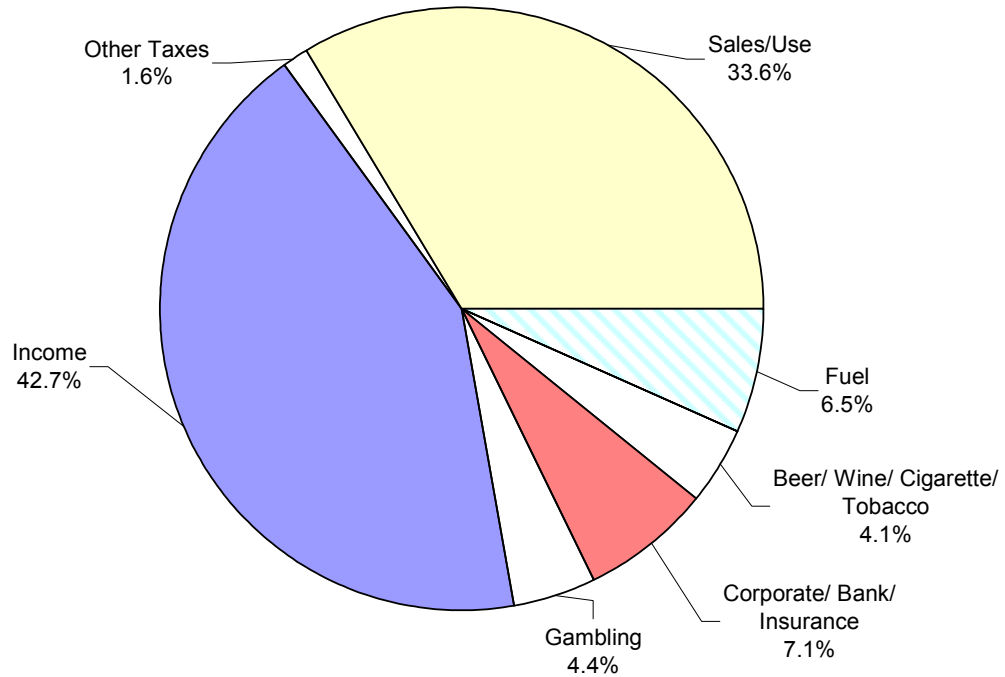
The average reading for Iowa non-farm employment over the 12 months ending October 2008 is 1,523,600, and net State tax receipts over the same 12 months totaled \$6.746 billion, or \$4,427 per non-farm job. This is \$642 (17.0%) higher than the per-job average for June 2005. Over that same time period, inflation (CPI-U) increased 11.3%. Therefore, tax revenue per job has exceeded the rate of inflation since June 2005 by roughly 1.7% per year. The following chart provides an historical perspective of tax collections per non-farm job and inflation-adjusted collections per job.



Net State Tax Revenue - Twelve Months Ending October 2008

Net Revenue = \$6.746 Billion

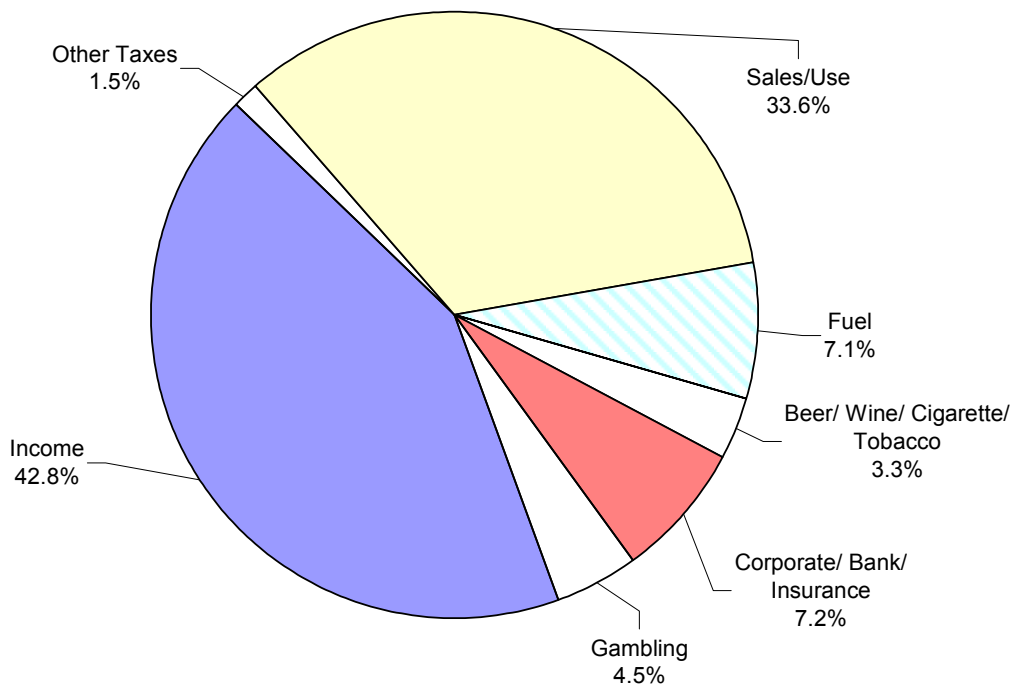
Percentages may not add to 100% due to rounding



Net State Tax Revenue - Twelve Months Ending October 2007

Net Revenue = \$6.364 Billion

Percentages may not add to 100% due to rounding



Net Tax Revenue Deposited to State Funds - Cash Basis

Dollars in millions - Columns and Rows may not add due to rounding

| Net Tax by Tax Type | Previous 12-Month Period Total | Most Recent 12-Month Period Total | 12-Month \$ Change | 12-Month % Change | Month of October 2007 | Month of October 2008 | October \$ Change | October % Change |
|---------------------------------|---|--|-------------------------------|------------------------------|----------------------------------|----------------------------------|------------------------------|-----------------------------|
| Banking | \$ 33.8 | \$ 33.2 | \$ - 0.6 | -1.8% | \$ 3.4 | \$ 3.6 | \$ 0.2 | 5.9% |
| Beer & Wine | 20.4 | 21.0 | 0.6 | 2.9% | 1.5 | 1.6 | 0.1 | 6.7% |
| Cigarette & Tobacco | 186.7 | 253.8 | 67.1 | 35.9% | 22.6 | 23.4 | 0.8 | 3.5% |
| Corporate Income | 326.2 | 336.7 | 10.5 | 3.2% | 26.4 | 3.8 | - 22.6 | -85.6% |
| Fuel | 454.6 | 440.9 | - 13.7 | -3.0% | 42.8 | 40.8 | - 2.0 | -4.7% |
| Gambling | 286.5 | 299.8 | 13.3 | 4.6% | 23.4 | 29.1 | 5.7 | 24.4% |
| Individual Income | 2,726.2 | 2,879.2 | 153.0 | 5.6% | 208.9 | 199.3 | - 9.6 | -4.6% |
| Inheritance | 72.2 | 84.6 | 12.4 | 17.2% | 5.2 | 8.7 | 3.5 | 67.3% |
| Insurance | 97.6 | 107.3 | 9.7 | 9.9% | 0.0 | 0.0 | 0.0 | 0.0% |
| Other Taxes | 2.4 | 5.9 | 3.5 | 145.8% | 1.9 | 1.7 | - 0.2 | -10.5% |
| Real Estate Transfer | 18.2 | 16.5 | - 1.7 | -9.3% | 1.4 | 1.3 | - 0.1 | -7.1% |
| Sales/Use | 2,138.9 | 2,266.7 | 127.8 | 6.0% | 134.8 | 144.0 | 9.2 | 6.8% |
| Total Net Taxes | \$ 6,363.7 | \$ 6,745.6 | \$ 381.9 | 6.0% | \$ 472.3 | \$ 457.3 | \$ - 15.0 | -3.2% |
| Gross Tax & Refunds | | | | | | | | |
| Gross Tax | \$ 7,022.1 | \$ 7,583.4 | \$ 561.3 | 8.0% | \$ 501.5 | \$ 531.4 | \$ 29.9 | 6.0% |
| Tax Refunds | \$ - 658.6 | \$ - 837.9 | \$ - 179.3 | 27.2% | \$ - 29.3 | \$ - 74.0 | \$ - 44.7 | 152.6% |
| Net Tax Receipts by Fund | | | | | | | | |
| State General Fund (GF) | \$ 5,388.3 | \$ 5,769.9 | \$ 381.6 | 7.1% | \$ 376.8 | \$ 360.8 | \$ - 16.0 | -4.2% |
| Road Use Tax Fund | \$ 708.0 | \$ 709.7 | \$ 1.7 | 0.2% | \$ 59.1 | \$ 61.7 | \$ 2.6 | 4.4% |
| Non-GF Gambling | \$ 226.5 | \$ 237.9 | \$ 11.4 | 5.0% | \$ 23.2 | \$ 26.7 | \$ 3.5 | 15.1% |
| Other State Funds | \$ 40.6 | \$ 28.1 | \$ - 12.5 | -30.8% | \$ 13.1 | \$ 8.1 | \$ - 5.0 | -38.2% |
| Local Option Taxes * | \$ 690.6 | \$ 734.8 | \$ 44.2 | 6.4% | \$ 47.4 | \$ 49.3 | \$ 1.9 | 4.0% |

* Sales, income, and hotel/motel. Distributed to local governments - not included in numbers above.

Numbers are rounded to the nearest \$0.1 million. Percentages are calculated after rounding.

Tax Categories Used in Table

Franchise (Bank) Tax: Taxes on banks are deposited to the State General Fund. State Credit Union Tax is included on this line also.

Beer & Liquor Tax: Taxes on beer, liquor, and wine are deposited to the State General Fund, the Liquor Control Fund, and a small amount is deposited to a Department of Economic Development fund for wine promotion.

Cigarette & Tobacco Tax: Cigarette and the tobacco products tax revenue is deposited to the State General Fund.

Corporate Income Tax: All Corporate Tax is deposited to the State General Fund.

Motor Vehicle Fuel Tax: All Motor Vehicle Fuel Tax is deposited to one of two road use funds, with the exception of tax revenue from the sale of aviation and marine fuels.

Gambling Tax: The first \$60.0 million of Gambling Tax revenue each fiscal year is deposited to the State General Fund. Other funds receiving deposits of Gambling Tax revenue over the last 24 months include the School Infrastructure Fund, the Rebuild Iowa Infrastructure Fund, The Gambler's Assistance Fund, the County Endowment Fund, the Endowment for Iowa's Health Account, and the Vision Iowa Fund.

Individual Income Tax: Most Individual Income Tax revenue is deposited to the State General Fund. Other destinations include the Workforce Development Fund (\$4.0 million) and Child Daycare Fund (\$2.6 million). In addition, several economic development programs are financed by individual income tax withholding. In those instances, the employer does not remit the tax withheld from employees and it is never deposited to a State fund. That revenue is not included here.

Inheritance Tax: All Inheritance Tax is deposited to the State General Fund.

Insurance Premium Tax: All Insurance Premium Tax is deposited to the State General Fund.

Other Taxes: Other taxes include Brucellosis Eradication Property Tax (deposited to a Department of Agriculture and Land Stewardship fund), Drug Stamp Tax (State General Fund), Utility Replacement Property Tax (State General Fund), and Car Rental Tax (Road Use Tax Fund). Other taxes also include a suspense account used to hold tax deposits prior to determining the correct tax type for the money and tax revenue transferred by the Department of Revenue to a separate account to fund tax collection activities (tax gap).

Real Estate Transfer Tax: Real Estate Transfer Tax is collected by counties. Counties retain 17.25% and remit the remainder to the State. The State deposits 95.0% to the State General Fund and 5.0% to the Shelter Assistance Fund.

Sales/Use Tax: General Sales/Use Tax is deposited to the State General Fund, while most Vehicle Use Tax is deposited to the Road Use Tax Fund. Beginning FY 2009, the Vehicle Use Tax was converted to a fee structure. To allow continuity of data, revenue from the fee structure is reflected in this document as tax revenue. Also beginning FY 2009, the School Infrastructure Local Option (SILO) Sales Tax was converted to a statewide 1.0% Sales/Use Tax and the revenue from that statewide tax is transferred out of the State General Fund monthly through a refund appropriation. To allow for continuity of data, the refund transfers are subtracted as part of the net Sales/Use Tax calculation.

Local Option Taxes: Local option taxes are presented at the bottom of the table and are not included in the numbers above. Prior to FY 2009, Local option taxes included the SILO Tax, Local Option Sales Tax (LOST) for local government finance, Local Option Income Surcharge for schools, and Hotel/Motel Tax. Starting FY 2009, the SILO Tax was converted to a 1.0% statewide tax and the SILO was eliminated. To allow for continuity of data, the transfers from the State General Fund as a result of the 1.0% statewide tax are included in the Local Option Tax amount.

Report Database

The database for this report is the State accounting system. If transactions are incorrectly coded in the system as tax revenue or tax refunds, the numbers presented here will be impacted.